

Message Text

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ACTION AF-06

INFO OCT-01 ISO-00 SS-15 SP-02 L-03 INR-07 EB-07 IGA-02

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FM AMEMBASSY KINSHASA

TO SECSTATE WASHDC PRIORITY 7329

C O N F I D E N T I A L SECTION 1 OF 2 KINSHASA 2981

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E.O. 11652: GDS

TAGS: EAID, EFIN, CG

SUBJECT: BALANCE OF PAYMENTS NEEDS: A LOOK AT THE ASSUMPTIONS
AND THE SOLUTION

BEGIN SUMMARY

1. ARRIVAL OF THE RECENTLY RELEASED IMF REPORT ON ZAIRE
(#EBS/76/129) WHICH CONTAINS THE FUND'S CALCULATIONS OF ZAIRE'S
FINANCIAL SITUATION PROMPTS US TO COMMENT UPON SOME OF ITS
ASSUMPTIONS AND THE ROLE WHICH ZAIRE'S CREDITORS AND BENE-
FACTORS WILL HAVE TO PLAY DURING THE COMING MONTHS. AFTER STUDY-
ING THE REPORT WE HAVE CONCLUDED THAT THE FUND OVERESTIMATES THE
EXPORT RECEIPTS WHICH ZAIRE WILL EARN DURING 1976, WHILE UNDER-
STATING THE QUANTITY OF IMPORTS REQUIRED TO PUT ZAIRE BACK ON
THE ROAD TO A HEALTHY ECONOMY. AS A RESULT, WE ESTIMATE ZAIRE
WILL FACE A \$657 MILLION FX DEFICIT, COMPARED WITH THE IMF'S
CALCULATION OF A \$300 MILLION DEFICIT. GIVEN THIS SITUATION, BOTH
DEBT RESCHEDULING AND ADDITIONAL BALANCE OF PAYMENTS ASSISTANCE
MAY BE NECESSARY TO BRIDGE THE GAP WHICH ZAIRE WILL PROBABLY
DEVELOP DURING 1976 BETWEEN FX RECEIPTS AND EXPENDITURES.
END SUMMARY.

2. EXPORT RECEIPTS, AS PROJECTED IN THE IMF REPORT, ARE BASED ON
UNREALISTIC REVENUE ESTIMATES FOR COPPER AND CRUDE OIL EXPORTS.
THE FUND OVERESTIMATES COPPER EXPORT RECEIPTS DUE TO FAULTY AS-
SUMPTIONS CONCERNING QUANTITY (500,000 MT) AND PRICE (66CT/LB.).

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THE QUANTITY OF COPPER WHICH ZAIRE CAN EXPECT TO SELL DURING

1976 IS DEPENDENT UPON BOTH PRODUCTION LEVELS AND TRANSPORTATION DIFFICULTIES, AS ZAIRE RECEIVES NO MONEY FOR ITS COPPER UNTIL IT IS LOADED ABOARD SHIP IN AN OCEAN PORT.

A. COPPER PRODUCTION: PRODUCTION LEVELS DURING 1976 ARE UNLIKELY TO DUPLICATE LAST YEAR'S LEVEL, WHEN GECAMINES PRODUCED ABOUT 460,000 MT, SHIPPED ABOUT 470,000 MT (PRODUCTION PLUS VIRTUALLY ALL OF GECAMINES' STOCKPILE), AND RECEIVED PAYMENT FOR ABOUT 430,000 MT. SODIMIZA, THE JAPANESE-OWNED COPPER CONCENTRATE PRODUCER, SUFFERED SERIOUS PROBLEMS DUE TO THE TRANSPORTATION DIFFICULTIES, AND PRODUCTION DWINDLED. SODIMIZA ONLY PRODUCES ABOUT 35,000 MT OF COPPER CONTENT PER YEAR AT MAXIMUM LEVELS AND OUR BEST INFORMATION INDICATES THAT PRODUCTION DURING 1976 WILL BE FAR BELOW THOSE LEVELS. AS SODIMIZA MAY SUFFER FROM SERIOUS TRANSPORTATION DIFFICULTIES DUE TO ITS PROBLEMS IN TRANSPORTING CONCENTRATES, WE EXPECT ITS CONTRIBUTION TO ZAIRE'S BALANCE OF PAYMENTS TO BE IN THE \$25 MILLION RANGE WITH A MAXIMUM OF 25,000 MT OF COPPER CONTENT EXPORTED. IN CONTRAST, GECAMINES, AS ZAIRE'S MAJOR MINERAL PRODUCER, IS CRUCIAL FOR THE COUNTRY'S ECONOMY. DURING 1975 GECAMINES WAS UNDER ORDERS TO MAXIMIZE PRODUCTION IN ORDER TO PROVIDE THE COUNTRY WITH FX. THESE DEMANDS FOR INCREASED PRODUCTION COINCIDED WITH THE ARRIVAL OF SUBSTANTIAL OPERATING PROBLEMS OCCASIONED BY THE FX SHORTAGE WHICH CAUSED A SHORTAGE OF SPARE PARTS AND PETROLEUM PRODUCTS. TO COMPENSATE FOR THESE DIFFICULTIES GECAMINES RESORTED TO MEASURES WHICH BOOSTED ITS 1975 PRODUCTION AT THE COST OF REDUCED PRODUCTION IN SUBSEQUENT YEARS. FOR MORE THAN HALF OF 1975 GECAMINES UNDERTOOK NO OVERBURDEN STRIPPING FOR ITS OPEN-PIT MINES, PREFERRING INSTEAD TO SAVE ITS INSUFFICIENT DIESEL FUEL SUPPLY FOR OPERATION OF THE MINING BINS WHICH CARRY THE PRODUCTION. AS A RESULT THERE MAY COME A PHASE WHEN GECAMINES WILL HAVE TO SLOW PRODUCTION DUE TO INADEQUATE PREVIOUS OVERBURDEN REMOVAL. LIKEWISE, GECAMINES CHOSE DURING 1975 TO EXPLOIT ITS RICHEST AVAILABLE ORE BODIES IN ORDER TO MAXIMIZE PRODUCTION AT THE LEAST COST. THIS PRACTICE WILL LEAD, HOWEVER, TO LOWER AVERAGE YIELDS DURING SUBSEQUENT YEARS. PRODUCTION DECLINE MAY ALREADY HAVE BEGUN. UNOFFICIAL BUT RELIABLE SOURCES REPORT THAT GECAMINES COPPER PRODUCTION WAS 69,000 MT DURING THE FIRST TWO MONTHS OF 1976, WHICH LEADS TO AN ANNUALIZED COPPER PRODUCTION OF ONLY 414,000 MT.

B. TRANSPORTATION PROBLEMS IN 1975 WERE HIGHLIGHTED BY THE CONFIDENTIAL

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CLOSURE OF THE BENGUELA RAILROAD. MEASURES TAKEN TO REDIRECT THE COPPER WHICH WOULD HAVE BEEN ROUTED THROUGH ANGOLA REQUIRED LONGER ROUTES AND AS A RESULT 30,000 MT OF COPPER WERE ADDED TO THE EXPORT PIPELINE. SINCE THEN, THE MOZAMBIQUE-RHODESIA BORDER HAS CLOSED, REMOVING ONE OF ZAIRE'S ALTERNATIVE ROUTES. REOPENING OF THE BENGUELA RAILROAD REMAINS PROBLEMATIC, AND THE TENUOUS EXPORT ROUTES THROUGH ZAMBIA, SOUTHERN RHODESIA, MOZAMBIQUE, AND SOUTH AFRICA REMAIN UNTRIED, FOR THE MOST PART. WE EXPECT ZAIRE WILL

PROBABLY DELIVER FOR EMBARKATION ABOUT 460,000 MT OF COPPER DURING 1976.

C. WE BELIEVE THAT THE IMF ASSUMPTION OF 66CT/LB. FOR THE AVERAGE PRICE OF COPPER DURING 1976 IS TOO HIGH. THE IMPORTANCE OF A REALISTIC PRICE ESTIMATE IS EMPHASIZED BY THE FACT THAT A ONE CENT DIFFERENCE IN THE AVERAGE ANNUAL PRICE OF COPPER CAUSES A DIFFERENCE OF \$10 MILLION IN ZAIRE'S EXPORT REVENUES. WE CALCULATE THAT THE AVERAGE PRICE OF COPPER ON THE LONDON METAL EXCHANGE FOR THE FIRST QUARTER OF 1976 WILL BE ABOUT 56 CT/LB. FOR 1976 COPPER PRICES TO AVERAGE 66 CT/LB., IT WILL BE NECESSARY FOR COPPER TO AVERAGE 69 CT/LB. DURING THE LAST NINE MONTHS OF 1976. DESPITE THE RISE IN COPPER PRICES DURING MARCH 1976, THE LEVELS OF STOCKS WHICH ARE REPORTEDLY IN EXISTENCE WOULD SEEM TO DISCOURAGE SUCH A RAPID RISE TO THE 69 CT LEVEL. MOREOVER, AN INCREASE IN PRICE DOES NOT BENEFIT ZAIRE UNTIL AFTER A DELAY OF THREE MONTHS, SINCE THE ADVANCE WHICH ZAIRE RECEIVES WHEN COPPER IS LOADED ABOARD SHIP IS BASED ON THE AVERAGE OF THE PREVIOUS THREE MONTHS' LME COPPER PRICE. WE PREFER TO PROJECT A REALISTIC PRICE OF 60 CENTS PER POUND AVERAGE 1976 COPPER PRICE.

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TO SECSTATE WASHDC PRIORITY 7330

C O N F I D E N T I A L SECTION 2 OF 2 KINSHASA 2981

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D. CRUDE OIL EARNINGS: THE IMF INCORRECTLY ASSUMES EARNINGS OF \$100 MILLION FROM ZAIRE'S CRUDE OIL EXPORT IN 1976, APPARENTLY BASED ON A PRICE OF \$11 PER BARREL AT THE PRODUCTION LEVEL OF 25,000 BPD. THE 25,000 BPD WAS THE ORIGINAL PRODUCTION LEVEL FORESEEN BY GULF; HOWEVER, RECENT ESTIMATES HAVE RAISED THE EXPECTED PRODUCTION LEVEL TO AN ANNUAL AVERAGE OF 30,000 BPD. BUT THE EXPLORATION AGREEMENT BETWEEN GULF AND THE GOZ GIVES GULF THE

RIGHT TO DRAW OFF 81.5 PER CENT OF THE PROCEEDS FROM CRUDE OIL SALE, WHICH LEAVES ONLY \$22.4 MILLION TO BE REPATRIATED TO ZAIRE.

E. IF WE BUY THE IMF ASSUMPTIONS ABOUT THE REMAINDER OF ZAIRE'S EXPORTS, THEN ZAIRE'S EXPORT EARNINGS LOOK LIKE THIS:

COPPER	\$608 MILLION
PETROLEUM	\$ 22 MILLION
OTHER (IDENTICAL WITH IMF)	\$373 MILLION

TOTAL \$1,003 MILLION

IN THIS COMPUTATION WE PRESUME PAYMENT FOR 460,000 MT OF COPPER AT \$0.60 PER POUND AVERAGE PRICE FOR 1976, AND PROCEEDS FROM CRUDE OIL EXPORT OF \$22.4 MILLION. THUS, WE ESTIMATE \$197 MILLION LESS IN EXPORTS FOR ZAIRE DURING 1976 THAN DOES THE IMF.

3. OUR DIFFERENCES WITH THE IMF STEM NOT ONLY FROM THE INCOME BUT ALSO FROM THE EXPENDITURE SIDE. THE IMF PROJECTS 1976 IMPORTS AT \$1 BILLION WHILE OUR ESTIMATES OF ZAIRE'S IMPORT NEEDS HAVE RANGED BETWEEN \$1.1 BILLION AND \$1.3 BILLION. WE NOTE THAT EVEN IN 1975, WHEN INDUSTRY WAS SEVERELY HINDERED FOR LACK OF SPARE
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PARTS AND RAW MATERIALS, TOTAL IMPORTS WERE AT LEAST \$1.057 BILLION. THIS LEVEL OF IMPORTS WAS CLEARLY IN-SUFFICIENT TO MEET THE NEEDS OF THE ECONOMY AND CONTRIBUTED TO NEGATIVE REAL ECONOMIC GROWTH. INDUSTRIAL GOODS PRICES WILL BE HIGHER IN 1976 THAN DURING 1975 SO A NOMINAL \$1 BILLION WILL BUY EVEN FEWER IMPORTS THAN IT WOULD HAVE LAST YEAR AND SIGNIFICANTLY LESS THAN THE QUANTITY OF MERCHANDISE ACTUALLY IMPORTED DURING 1975. ALL THINGS BEING EQUAL, THE RESULT OF A DECISION TO RESTRICT IMPORTS TO \$1 BILLION IN 1976 WILL BE AN EQUALLY POOR OR WORSE ECONOMIC PERFORMANCE IN 1976 THAN IN 1975. BASED ON PAST IMPORT TRENDS AND OUR DISCUSSIONS WITH LOCAL BUSINESSMEN OF THEIR IMPORT NEEDS, WE ESTIMATE THAT \$1.180 BILLION WOULD BE THE MINIMUM LEVEL OF FOREIGN IMPORTS CONSISTENT WITH THE REESTABLISHMENT OF A POSITIVE ECONOMIC GROWTH RATE IN 1976. ALTHOUGH ADEQUATE DATA ARE NOT AVAILABLE, WE WOULD ESTIMATE THESE IMPORT NEEDS AS FOLLOWS:

POL	\$170 MILLION
CONSUMER GOODS	\$360 MILLION
OF WHICH	
(FOOD GRAINS)	\$(60) MILLION
(OTHERS)	\$(300) MILLION
GEAMINES	\$100 MILLION
CAPITAL GOODS	\$250 MILLION
RAW MATERIALS	\$300 MILLION

TOTAL \$1,180 MILLION

THUS WE PROJECT IMPORT LEVELS SHOULD BE AIMED AT \$1,180 MILLION, OR \$180 MILLION GREATER THAN THE IMF HAS PLANNED.

4. USING OUR EXPORT AND IMPORT ASSUMPTIONS, ZAIRE'S 1976 BALANCE

OF PAYMENTS DEFICIT LOOKS LIKE THIS:

- A. \$100 MILLION DEFICIT SHOWN IN IMF REPORT
- B. \$177 MILLION ADDITIONAL DEFICIT USING OUR EXPORT PROJECTIONS (PARA 2)
- C. \$180 MILLION ADDITIONAL DEFICIT USING OUR IMPORT PROJECTIONS (PARA 3)
- D. \$200 MILLION PORTION OF DEBT SERVICE DUE WHICH IMF ASSUMED WOULD BE RESCHEDULED
- E. \$657 MILLION TOTAL EXPECTED DEFICIT (SUM OF A, B, C AND D)
- F. \$223 MILLION RELIEF DUE TO \$163 MILLION IMF AND \$60 MILLION USG ASSISTANCE

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- G. \$434 MILLION RESIDUAL DEFICIT TO BE FINANCED BY DEBT RESCHEDULING AND BALANCE OF PAYMENTS ASSISTANCE

5. SHOULD WE BE WRONG AND THE IMF RIGHT, WE THINK SHORT TERM BALANCE OF PAYMENTS SUPPORT SHOULD BE CONSIDERED AS AN ALTERNATIVE TO DEBT RESCHEDULING. IN THIS CASE ZAIRE'S TOTAL EXPECTED DEFICIT WOULD BE AS FOLLOWS:

- A. \$100 MILLION DEFICIT SHOWN IN IMF REPORT
- B. \$200 MILLION PORTION OF DEBT SERVICE DUE THAT IMF ASSUMED WOULD BE RESCHEDULED
- C. \$300 MILLION TOTAL EXPECTED DEFICIT
- D. \$223 MILLION RELIEF DUE TO \$163 MILLION IMF AND \$60 MILLION USG ASSISTANCE
- E. \$ 77 MILLION RESIDUAL FX DEFICIT TO BE FINANCED BY DEBT RESCHEDULING OR BALANCE OF PAYMENTS ASSISTANCE

UNDER THE IMF ASSUMPTIONS THEN, ZAIRE'S RESIDUAL DEFICIT WITH NO RESCHEDULING WOULD AMOUNT TO ONLY \$77 MILLION. WHAT WOULD BE THE BEST METHOD OF FINANCING THIS DEFICIT? DEBT RESCHEDULING WOULD INVOLVE LENGTHY NEGOTIATIONS AND POSSIBLY ONEROUS TERMS. ZAIRE'S CREDIT RATING WOULD UNDOUBTEDLY BE FURTHER DAMAGED. IN CONTRAST, ADDITIONAL BALANCE OF PAYMENTS SUPPORT OF \$77 MILLION WOULD ALLOW ZAIRE TO FINANCE ITS DEFICIT ON LESS ONEROUS TERMS WHILE AVOIDING THE DAMAGING PROCESS OF DEBT RENEGOTIATION RESCHEDULING NEGOTIATIONS.

6. IF, HOWEVER, THE EMBASSY'S CALCULATIONS ARE IN THE BALL PARK, ZAIRE'S RESIDUAL DEFICIT WILL BE BIG ENOUGH TO REQUIRE BOTH SUBSTANTIAL BALANCE OF PAYMENTS SUPPORT AND DEBT RESCHEDULING. IF WE AGREE WITH THE IMF THAT \$200 MILLION IN 1976 DEBT PAYMENTS BE RESCHEDULED, THERE WILL REMAIN \$234 MILLION TO BE FINANCED IF IMPORT LEVELS ARE TO BE HIGH ENOUGH TO PERMIT AN EFFECTIVE ECONOMIC RECOVERY. TO THE EXTENT POSSIBLE, WE THINK BALANCE OF PAYMENTS SUPPORT IS PREFERABLE TO DEBT RESCHEDULING AS A MEANS OF FINANCING ZAIRE'S RESIDUAL DEFICIT SINCE HEAVY DEBT RESCHEDUL-

ING WOULD PROBABLY TEND TO PUSH DEBT PAYMENTS TO 1977 AND 1978
WHEN ZAIRE'S DEBT SERVICE BURDEN IS ALREADY LARGE.

7. EMBASSY HAS NO OBJECTION SHOULD DEPARTMENT WISH TO PASS
FOREGOING TO OTHER USG AGENCIES.
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